In some cases, the Commission has shown a disturbing willingness to ignore present economic facts in favor of a rosy vision of coming competition. For example, in the City of Boston in 2001, the Commission relied on build-out schedule commitments by overbuilder RCN to support a conclusion that there would be soon be competition everywhere in the City, concluding in effect that the Commission might as well deregulate now.[66] This reliance on a four-year-old build-out schedule, however, ignored the facts of the more recent downturn in the telecommunications industry,[67] the specific financial difficulties faced by RCN,[68] the

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of the franchise areas, and incumbent cable operator has responded competitively in anticipation of the LEC competition.).” *See Effective Competition Order* at n.45.

[66] “In order to establish the presence of effective competition, a cable operator need not prove that a competing LEC is providing service throughout its service area. Instead, if the LEC is franchised, a showing regarding the coverage and construction obligations in the franchise agreement normally is sufficient. . . . To the contrary, RCN’s testimony supports the Bureau’s conclusion that RCN *intends* to build out its system to serve the entire city of Boston, albeit at a slower pace than it originally intended.” *In re Cublevision of Boston, Inc., Petition for Determinution of Effective Competition, Application for Review,* Memorandum Opinion and Order, 17 FCC Rcd. 4772, ¶¶ 9, 14 (2002) *(“Boston Review Order”)* (emphasis added).

[67] ***See**, e.g.*, Mavis Scanlon, *RCN: After the Fall,* Cable World, Jan. 1, 2001 at 4 (“The pullback in the capital markets ‘definitely is going to affect every overbuilder”’); Lee Bergquist, ***New** Cable Company Pulling Plug; Digital Access Cites Inability to Raise Capital,* Milwaukee Journal Sentinel, Mar. 3, 2001, at 1D (“when financing is drying up for many companies that want to build cable systems in markets where there is existing cable operator.”).

[68] *See, e.g.*, Andrea Estes, *For Cable Rival, No Room at the Poles: Current Utility Providers Reluctant to Add RCN,* The Boston Globe, Dec. 17, 2000, at 1 (South Weekly Ed.) (“But now – two years after RCN signed deals with Quincy, Weymouth, and Randolph – RCN officials last week said they aren’t even close to being ready to go.”); Tom Kirchofer, *Media Upstart Fires* 65, The Boston Herald, Jan. 23, 2001, at 25 (“RCN spokeswoman Nancy Bavec said “...we’re going to be expanding in the Boston market at a lesser rate of growth then previously”); Len Boselovic, *AT&T Woes Hurt C-COR Stock’s Reception,* Knight-Ridder Tribune Business News, Jan. 8, 2001, at B-7 (“RCN Corp. (RCNC) announced last month it would spend only about $775 million next year, 50 percent lower than its original budget”); Bruce Mohl, *Cable TV Mergers Delaying Rate Hikes, Big Firms Have Yet To Announce Plans*

company's slowdown in construction in Boston in particular.[69] and explicit statements by KCN that it would not be able to meet its build-out schedule in Boston."' As a result, the Commission declared victory and decreed effective competition, even though the majority of the City's subscribers had no choice of cable operator

The postscript to the Commission's decision in the Boston matter is particularly galling. Thirty-five days after the Commission's decision, RCN requested to be certified as an OVS operator for the City of Boston." Four days later, RCN notified the City that no money for new construction in Boston would be budgeted in 2002 or 2003, and further requested "relief from its franchise obligations." In the interest of promoting competition and competitive choice for the City's residents, in October 2002, the City of Boston reluctantly agreed to terminate RCN's franchise and grant RCN an OVS license. The OVS license does not contain build-out requirements, although it does require that if and when RCN is able to budgei money to begin new construction in Massachusetts, 50% of those dollars will be spent in Boston. Thus, the build-out requirement on which the Commission premised its premature declaration of effective competition no longer exists

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for Corning Year, Boston Globe, Dec. 26, 2000, at C1 ("RCN, which is building a network from the ground up in Greater Boston, has been experiencing financial difficulties lately").

[69] *In re Cablevision of Boston, Inc., Petition for Determination of Effective Competition,* Application for Review of Determination of Effective Competition *in re* Cablevision of Boston, Inc., Exhibit 2 [RCN Construction Schedule (March 13, 2001)] (filed Aug. 20, 2001) *("Boston Application for Review").*

[70] *Boston Application for Review* at 3-4, Exhibit 1 [Thomas Steel, Vice-president and Regulatory Counsel for RCN, Testimony at Annual Performance Review of RCN BECO LLC (March 14, 2001)] at 7, 8, 10.

[71] Open Video System Certification Application of RCN BecoCom, LLC (filed April 18, 2002), *available ut* http:l/www.fcc.gov/mblovs/rcnbos.doc (last visited 11/4/02)

However, since the Commission's effective competition decision, AT&T has attempted to avoid truing-up its 2000 rates, arguing that the 2001 effective competition determination, based on the now-void 1999 RCN franchise agreement, stripped the City of authority to regulate rates or order refunds as of the date of Cablevision's original 1997 Petition for Determination of Effective Competition.[72] In addition, after agreeing not to raise rates as a condition of the City's approval of the AT&T-Comcast merger and franchise transfer, AT&T-Comcast attempted to impose a $3.00 hike in the form of an equipment rate increase.[73]

It is understandable to look forward to the replacement of rate regulation rules by robust competitive forces. But a promise of competition is not the same as actual competition. Wishful thinking cannot be allowed to drive the Commission's response to its congressional mandate. That was the problem with the 1984 Act's premature elimination of rate regulation; it was why the 1992 Act's restoration was necessary; and it requires the Commission to act now on facts, not merely hopes.

B. Recommendations

The Commission should revise its rules to ensure that they yield a determination of effective competition only where two providers actually offer service to the same subscriber.

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[72] Letter from James White, Jr, Senior Attorney, AT&T Broadband, to Alicia Matthews, Director, Massachusetts Department of Telecommunications & Energy Cable Television Division, 3-4, (Sept. 14, 2001) ***("Any*** order adopted after the Bureau's effective competition decision that prescribes rates or refund payments, ***even for a time before*** *July* 20, *2001,* would constitute rate regulation that is now precluded in the City (emphasis in original), *citing In **re Time Warner Cable,*** Refund Plan, 13 FCC Rcd. 17679 at ¶ 2 (1998) ("conditioning enforcement of a rate refund plan on the FCC's denial of a cable operator's petition for effective competition").

The operator who wishes to be freed from rate regulation must show that all subscribers in the area to be declared competitive actually have competitive alternatives. Any subscribers who do not have these alternatives should have the right to continue to invoke rate regulation on their behalf, if the local community is willing to continue it. The cable operator must show that the programming offered is in fact comparable in content to the basic cable tier, and that any data used in this showing have been verified by the cable operator. The burden must remain on the cable operator to show these facts, in accordance with the congressional findings underlying the statute.[74]

The Commission should rescind the rule that considers DBS to constitute a competitive alternative everywhere, and decline to find effective competition based solely on DBS. The Commission's own findings, along with those of the **GAO,** make clear that the existence of DBS does not in fact restrain cable rates and hence make rate regulation unnecessary. Until it can be shown that DBS competition has the same power to produce reasonable rates as wireline competition, the Commission cannot treat DBS as a competitive alternative for purposes of rate regulation.

To provide a reasonable chance to "vet" questionable data that may be submitted, the Commission should consider requiring cable operators to submit an effective competition petition to the local franchising authority *first*, so that the alleged facts can be examined by

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[73] Karen E. Crummy, *City **Fumes** at **Cable** TV Rate Hike*, Boston Herald, Aug. **16,** 2002.

[74] The cable operator should also be required to avoid including large quantities of unnecessary data – for example, printouts showing data for every city in the state, rather than just those for which the filing is made – to minimize paperwork and improve the ability of the Commission and the local franchising authority to identify the pertinent facts.

those familiar with local conditions, and having the local franchising authority then submit the petition, with its comments, to the FCC. This would parallel the approach the Commission used earlier for CPS tier rate complaints, so that the Commission need not "begin its proceeding with less than a complete record."[75] It would also conform to the original procedure the Commission envisioned for effective competition claims, under which the operator would go to the local community first and approach the FCC only if the local community did not agree to the petition.[76] In this way the Commission could stand a reasonable chance of getting a more complete record and hence making an accurate finding regarding effective competition.

IV. THE COMMISSION HAS ALLOWED OPERATORS TO USE CHANNEL MOVEMENT TO CHARGE SUBSCRIBERS FOR CHANNELS THEY DO NOT RECEIVE.

A. Problem

A problem has developed in the last several years with respect to the apparently simple matter of moving channels out of the basic tier.[77] In at least some cases, cable operators have sought to take advantage of the Commission's rules to continue charging subscribers for channels they do not receive. The result is a telling case study of the cable industry's willingness to distort the Commission's rules to evade the Commission's prescribed methodology for rate regulation,

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[75] ***Effective Competition Order*** at ¶ 41.

[76] ***See*** former 47 C.F.R. § 76.915 (prior to 1999); Effective Competition at ¶ 30.

[77] ***See*** *NPRM&O* at ¶¶ 12-23, 55.

The Commission's original benchmark rules set a per-channel rate for the basic tier that was deemed to recover all the costs associated with providing a channel to subscribers – both channel-specific costs, such as payments to programmers. and an allocated share of the cost of building and running the cable system as a whole.[78] When a cable operator *removed* a channel from the basic tier, it was thus necessary to back out of the basic tier rate all the costs associated with that channel. Those identifiable costs that were specific to the channel, such as programming costs, could be removed directly. This left the channel's share of the overall network costs, referred to as the "residual," which also had to be removed from the basic tier rate. If this were not done, the basic subscriber would end up continuing to pay part of the cost of a channel no longer carried on the basic tier.[79]

This basic principle was followed for a number of years without significant comment, though in at least one case the Commission did have reason to indicate that its rules required moving the residual, as well as the external costs, when a channel was moved among tiers.[80] The specific mechanism for this removal of the residual had to be changed, however, due to

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[78] *See, e.g., In re Falcon Cable Systems Company, Appeal from a Local Rate Order of the County of San Luis Obispo, California,* Memorandum Opinion and Order, 14 FCC Rcd. 2105, ¶ 7 (1999) ("[T]he benchmark system presumes that the rate charged allows recovery of capital costs"; *In re TCI of Southwest Mississippi, Appeal of Local Rate Order of the City of Ocean Springs, Mississippi,* Memorandum Opinion and Order, 10 FCC Rcd. 8728, n.30 (1995) ("The benchmark rates . . . internalize any other system variances that existed at the time of the survey, such as the carriage of revenue-producing channels").

[79] *See Second Reconsideration Order* at ¶¶ 174-175 (1994).

[80] *See TCI Cablevision of Dallas, Inc., Request for Stay of Local Rate Order of the City of Farmers Branch, Texas,* Memorandum Opinion and Order, DA 99-1159, 14 FCC Rcd 9252 at ¶¶ 3-4, 7, n.3 (1999) *("Farmers Branch Order")* (granting stay based in part on a conclusion that moving the residual with the channel complied with "the methodology provided in the form and that we have accepted in CPST cases before the Commission").

the Commission's adoption of programming incentives that increased the costs the operator could charge for added channels. When the Commission added these cable operator bonuses in its *Sixth Reconsideration Order* in 1994, it specified that they were to be temporary options, ending on December 31, 1997.[81] However, the Commission wrote the sunset provision for these programming incentives in such a way that an incautious reader might suppose that the *entire* rule for moving the residual (§ 76.922(g)) would sunset on that date.[82]

The only rational way to read this provision is to conclude that the intent of the Commission was to sunset only the new provisions, not all of § 76.922(g). It appears that the previously existing rule (including the residual rule) was then to return and replace the newly-amended rule. The two new methods added in the *Sixth Reconsideration Order* did not take the place of the entire subsection (g). There is no indication in that order that the expiration of these temporary subparagraphs was intended to take the rest of subsection (g) with them (Indeed, if it did so, there would be *no* way under the Commission's rules to adjust rates when channels are moved or deleted.) Yet, the language of § 76.922(g)(8) anomalously appeared to refer to all of § 76.922(g), rather than solely the new provisions, § 76.922(g)(3) and (g)(7).

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[81] *In the Matter of Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation,* MM Docket 92-266, Sixth Order on Reconsideration, Fifth Report and Order, and Seventh NPRM, 10 FCC Rcd 1226, at ¶ 98 (1994) *("Sixth Reconsideration Order").*

[82] "*The new rule* for adjusting rates when channels are added, deleted, or substituted on CPSTs will be in place through December 31, 1997, and will be reviewed prior to the end of that period to determine if there is any reason to continue to provide incentives to increase the number of channels on any CPST. *The new rule will expire on that date and will be replaced by our existing rule* unless it is reinstated by the Commission. The special streamlined cost-of-service procedure for headend equipment costs for small systems also will expire on December 31, 1997 unless it is reinstated by the Commission." *Id.* (emphases added).

It is possible that this appearance of over-inclusiveness was merely a typographical error, as suggested in the Commission's *Farmer's Branch* order[83] Or the Commission's drafters may have intended the language in (g)(8) to mean that when the "new and improved" subsection (g) sunset, subsection (g) would *revert to the former language of that section*, prior to any sunset requirements and without the *Sixth Reconsideration Order's* new adjustments. Certainly any responsible person who understood how the Commission's rules were supposed to work would have recognized that *some* means of removing the residual from the basic tier rate would have to survive. Otherwise, basic subscribers would still be required to pay residual amounts for a channel they no longer received.[84]

Subsequently, however, at least one cable operator – Time Warner – took the position that the Commission's rules allowed them to leave the entire residual amount in the basic tier rate. According to this claim, the Commission's sunset provision removed the residual rule altogether, leaving no rule at all for backing out the residual. Accordingly, Time Warner claimed, it could not be prevented from continuing to charge basic subscribers part of the cost for a channel they no longer received. Under this literalist reading of the Commission's rules, an operator could continue to remove channels from the basic tier one by one, without adjusting its rates accordingly.[85]

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[83] *Farmers Branch Order* at ¶ 4

[84] The converse is also true. In the absence of (g)(5), a cable operator that *added* a channel to the BST would not be allowed to *raise* its rates to incorporate the increased residual. One assumes, however, that the Commission's rules should not be read to *discourage* a cable operator from adding new programming.

[85] Or, conversely, it could add channels, one by one, and yet be unable to recover the full value of the channel in an adjusted rate.

In 2001, Time Warner took the above position first in its rate filings, then in discussions with a local franchising authority, then in at least one appeal of the franchising authority's rate order to the Commission.[86] In that case, the double recovery Time Warner sought to capture through this technical pretext involved only a single channel. In other cases, however, the effect was more drastic. For example, the Miami Valley Cable Council, in Ohio, found that Time Warner had removed almost a third of the channels from the basic tier – nine out of 29 channels, or 31% less service – yet adjusted the rate only minimally. The principle, however, was the same: Time Warner was charging the basic subscriber for channels the basic subscriber did not receive."

It should be emphasized that this is a position that *could not* have been adopted by Time Warner in good faith. No cable operator could seriously believe that it should be allowed to continue charging subscribers for a channel it had taken away. Yet Time Warner not only insisted on this absurd position before the local franchising authority, but insisted on appealing the community's rate order to the Commission, causing unnecessary costs for the Commission, the local franchising authority, and the company.

[86] *See In re Time Warner Entertainment-Advance/Newhouse d/b/a Time Warner v. Southwestern Oakland Cable Commission,* Opposition to Appeal of Local Rate Order (tiled Oct. 21, 2002); *In re Time Warner Entertainment-Advance/Newhouse d/b/a Time Warner v. Southwestern Oakland Cable Commission,* Reply to Opposition to Motion to Dismiss Appeal of Local Rate Order (filed Aug. 12, 2002); *In re Time Warner Entertainment-Advance/Newhouse d/b/a Time Warner v. Southwestern Oakland Cable Commission,* Motion to Dismiss Appeal of Local Rate Order (filed July 29, 2002); *In re Time Warner Entertainment-Advance/Newhouse d/b/a Time Warner v. Southwestern Oakland Cable Commission,* Opposition to Appeal of Local Rate Order (filed Nov. 1, 2002). The Southwestern Oakland Cable Commission's filings in that proceeding are incorporated by reference in these Comments.

[87] Time Warner could *also* recover the full cost of the former basic channel from its rates for the CPS tier to which it had been moved, leading to a double recovery.

The Commission's response on this issue is a textbook example of the failure to prevent evasions referred to above. In the *NPRM&O* itself, the Commission incorporated a complex single-paragraph ruling – the "Order" part of the *NPRM&O* – which appeared to be designed to address this problem. It seemed clear that this Order rejected the frivolous position Time Warner had taken, although it did not indicate that any sanctions would be applied against operators who had engaged in this abuse of the Commission's rules. Almost two months later, however, the Commission abruptly issued the Amending Order, rewriting the ordering paragraph of the *NPRM&O* (without explanation or clarification as to what the amendment was intended to accomplish). The resulting paragraph was still more complex and more obscure than the original. To the extent that a reader can understand its goal, however, it appears that the goal may be to allow **a** cable operator to "get away with" an incorrect methodology for channel movement (one which adjusts the residual, but differently from the way the original *NPRM&O* directed) if the operator had used that methodology before the date of the Amending Order.[88]

The only clue as to why the Commission would make this change, two months after the original order was issued, seems to be the following sentence added by the Amending Order:

> We recognize that some operators removing channels from the BST before this clarification may have read paragraph 98 of the *Going Forward **Order*** to allow

[88] This special exemption would not apply to Time Warner in the appeal referred to above, because Time Warner did not adopt the second methodology in its rate filing or its appeal. The company's rate filing and appeal took the frivolous position that *no* adjustment of the residual should be made. The second methodology appears to have been mentioned for the first time in Time Warner's Reply to the franchising authority's Opposition on the appeal

BST rate adjustments based on the per channel adjustment factors from the table in section 76.922(g)(2), and previously in 47 C.F.R § 76.922(e)(1994).[89]

Why would this fact, if true, he relevant? Presumably it is the Commission's job to tell cable operators how properly to read its rules, just as it tells franchising authorities how to do so in ruling on rate appeals. The only sense that can be given to the sentence quoted above appears to be that it represents a reappearance of the fallacy noted above in connection with à la carte tiers: the notion that an "honest mistake" by a cable operator is to be rewarded by allowing the mistake to stand."

In fact, even if there were evidence that a "mistake" by the operator were honest (a factor that is certainly absent in the position that no adjustment need be made to the residual), this would have no hearing whatsoever on the *correct formula to arrive at a reasonable rate.* Rate regulation is simply not a matter of rewarding good intentions, much less intentions that are quixotically presumed to be good even in the face of contrary evidence." It is a matter of protecting the subscriber against unreasonable rates; and allowing an operator's error to stand on the grounds that the operator *might conceivably have believed* it correct is a failure to prevent unreasonable rates and a failure to prevent evasions, both of which are violations of the Commission's express responsibilities under the statute."

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[89] *Amending Order* at ¶ *2*, amending paragraph 55 of the *NPRM&O*

[90] *See* n.32 *supra* and accompanying text.

[91] *See* n.31 *supra* and accompanying text.

[92] It is noteworthy that the Commission does not seem to apply the same standard to the actions of local franchising authorities, its co-regulators. No case appears to exist in which the Commission approved a local community's action on the grounds that the community *might* have believed it was applying the Commission's rules correctly – much less one where the

Correcting unreasonable rates is not a punishment. It merely achieves the statute's goal of protecting the subscriber. Correcting an erroneous assumption (even if it were made in good faith) by an operator is no more unfair than correcting a tax return in an audit to conform with applicable law. If the Commission's intent in the Amending Order were to "let off the hook" cable operators who had misapplied the Commission's rules, it would be facilitating evasions, not preventing them as required by Congress.

B. Recommendations

The fundamental recommendation on this issue is simple: The Commission should clarify beyond any doubt that, programming costs aside, moving a channel out of (or into) the basic tier means moving that channel's *pro rata* share of the tier cost - the residual.

A second recommendation, however, flows from the way in which this issue illustrates the ability of cable operators to profit when the rate regulation system does not work. The issue of the residual in channel movement was presented in one appeal at the Commission The same abuse of the Commission's rules, however, may have been embedded in any number of Time Warner's rate filings (not to mention those of other MSOs). If a cable operator is allowed to get away with a misapplication of the rules in every case that the local franchising authority does not catch, or lacks the resources to follow up on,[93] then the result will be an

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Commission approved a local action in the face of a finding that there was no apparent ,justification for the action other than to *avoid* the Commission's rules, as was true of the cable operators in the a la carte tier cases.

[93] Particularly in the knowledge that a cable operator is fully prepared to waste the community's limited resources through frivolous appeals.

undeserved windfall to the operator, in the form of unreasonable rates.[94] The Commission should adopt a rule, and implement it in every rate order issued on appeal, requiring that an operator who is found to have misapplied the Commission's rules must go back and correct that error in ***every*** rate filing that contains that error. Only in this way can evasions be discouraged, by removing the unearned benefit operators will otherwise derive from the ability to retain the fruits of their unappealed misuses of the rules

V. THE COMMISSION'S RULES ON NATIONAL EQUIPMENT RATES HAVE PROVEN IMPRACTICABLE TO ENFORCE.

A. Problem

Prior to 1996, cable operators were required to use local system data and equipment basket costs specific to the franchise area to arrive at equipment rates. This approach ensured that subscribers would pay only the real costs of the equipment actually available to them in that system, and utilized costs that could often he checked against local government records, such as property tax filings and subscriber counts. The 1996 Act. however, allowed cable operators to use aggregate costs to arrive at equipment rates, rather than costs specific to the franchise area:

> The Commission shall allow cable operators, pursuant to any rules promulgated under subsection (b)(3), to aggregate, on a franchise, system, regional, or company level, their equipment costs into broad categories, such as converter boxes, regardless of the varying levels of functionality of the equipment within each such broad category. Such aggregation shall not be permitted with respect

[94] Indeed, if this windfall were allowed, it would reduce the operator's net costs nationwide, and hence that decrease would need to be passed through at least annually in the form of rate ***reductions. See*** § 76.922(e)(2)(ii)(B).

to equipment used by subscribers who receive only a rate regulated basic service tier.[95]

The Commission amended its rules to reflect such aggregation in June. 1996.[96] Unfortunately, in implementing the statutory change, the Commission in practice allowed operators to aggregate in such a way as to impede review by local franchising authorities. National data are of course inherently more difficult for a local community to validate than data from the community itself. But this task became exponentially more difficult because of the ways in which operators were allowed to avoid providing accurate or even intelligible data.

The concept of reporting aggregate data seems to have been that this would make it easier for cable operators to assemble the necessary data, because the information could be aggregated at the same level where it was kept on the company's books. The Commission in fact required an operator to aggregate its data at the level where the operator kepi the data.[97] The first annual Form 1205 filing by TCI (as it then was) under the new rules, however, in March 1997, ignored all of this and instead relied on a so-called sampling technique. TCI picked a subset of its systems that it claimed were representative, averaged out the data from those systems alone, and submitted the results of this operation (not the underlying data) to

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[95] 47 U.S.C. § 543(a)(7)(A). The Commission had already ventured into this area in some of the "Social Contracts" it entered into with cable operators prior to 1996. *See, e.g.*, ***In** re Social Contract for Time Warner*, Memorandum Opinion and Order, 11 FCC Rcd. 2788 (1995).

[96] 47 C.F.R. § 76.923(a), (c), (f), (g), (m); ***In** re Implementation of Section 301(J) of the Telecommunications Act of 1996*, Report and Order, 11 FCC Rcd. 6778 (1996) *("EquipmentAggregation Order").*

[97] *See Equipment Aggregation Order at* ¶ 17; ***In** re TCI Cablevision of Nevada, Inc., Appeal of Local Rate Order of Washoe County, NV; City of Sparks, NV; City of Reno, NV; Carson City, NV*, Consolidated Order, 11 FCC Rcd. 14,378, ¶ 13 (1996).

local franchising authorities. Curiously, in many communities the results were far higher than the previous year's unaggregated maximum permitted rates for the very same equipment, even though the aggregation was supposed to be revenue-neutral. For example, in one community the maximum permitted rate for addressable converters was $1.87 in 1996; in 1997 TCI claimed the same type of converter had increased in cost to $3.54, an increase of 89%.

This approach was not consistent with the Commission's rules, which required total aggregate data, not a sample. But the Commission failed to enforce those rules effectively against TCI. Initially, in reviewing TCI's appeals of numerous local rate orders, the Cable Bureau did comment that TCI had not submitted sufficient information to show that its methodology represented a fair determination of costs, and noted that the burden had to be on TCI to do so, not on the city in question, which had no independent way of ascertaining TCI's costs.[98] However, on reconsideration, almost a year later, the Bureau vacated that section of the original order and remanded, apparently feeling that it *was* up to the city to show that TCI's methodology was incorrect.[99] As a result, it appears that in practice the Commission acceded to TCI's rewriting of the aggregation rules. The Commission acknowledged that the magnitude of the increase claimed by TCI using that methodology "may be a reason to closely examine supporting information,"[100] but it took no steps to do so, or to assist local communities in doing so.

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[98] *Richardson Order* at ¶¶ 26-30.

[99] *Richardson Reconsideration Order* at ¶¶ 24-25

[100] *Id.* at ¶ 24.

In fact, a closer examination at the local level revealed significant facts. TCI stated in response to one local data request that its total pool of converter costs reflected the gross book value for all converters, including fully depreciated converters, whether or not they were currently in service. That gross book value also included purchase price allocations recorded at the time the system was acquired. By contrast, in local records such as the company's personal property tax return, the actual number of converters in service on the assessment date was used. There were thus peculiarities, if not irregularities, in the accounting treatment of such equipment that were more effectively revealed by comparison to local records, once it was possible to convert TCI's aggregate data to numbers that could in fact be so compared.

The Commission's failure to demand true aggregation supported by corporate financial books and records, rather than just an operator-selected sampling, means that there is no way of knowing how the choice of sample communities may have been biased, whether the data used were consistent or sound, or whether the averaging methodology was valid. Yet, three years after the reconsideration order noted above, the Commission has taken no steps to address the problem.

It is possible that the Commission felt it could leave this matter to local authorities to resolve. If so, it underestimated the ability of operators to frustrate such resolution through "passive-aggressive" noncompliance. One financial expert working for local communities, for example, sought to investigate TCI's supporting data. The company's only response to specific questions was to ship large quantities of documents to the reviewer, without the requested explanations.“” While it is indeed essential to have the underlying data, forcing the reviewer in effect to try and re-create TCI’s results from this raw material, without detailed explanations and responses to specific questions, imposes enormous financial burdens on local franchising authorities and hence effectively prevents them from analyzing the data – a favorable result for the cable operator. Moreover, TCI impeded the effective or consistent application of any corrections by conditioning its submission of data on confidentiality commitments to prevent communities from sharing with others the details of their findings regarding national data, making it necessary for each community to re-invent the wheel.’”

A different approach was adopted by Time Warner. This company “aggregated” data not by taking multi-jurisdictional information from the books at a level where it was kept in aggregate form, but rather by having fifty participating systems compile data specific to that locality and send the information to Time Warner’s Connecticut office, where it was “consolidated” into aggregate figures.’”’ Review of the results indicated that the individual system data were not prepared using consistent methodologies to begin with, vitiating the Time Warner approach at the source. The franchising authority’s financial expert spent seven months asking for detailed support for the 2001 aggregate numbers. During that time Time Warner’s total response was one box of workpapers without cover letter or explanation. Finally, six weeks before the expiration of the twelve-month period allotted for review by the Commission, Time Warner delivered to the reviewer the original documents received by Time

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[101] Declaration of Garth Ashpaugh, CPA, attached as Exhibit 1 (“Ashpaugh Declaration”).

[102] Ashpaugh Declaration at ¶ 4

Warner's Connecticut office, without explanation, under a cover letter suggesting that the reviewer contact each of the fifty systems individually with any questions. (No contact information for these systems was provided with the letter.)[103]

Thus, the Commission's failure to establish firm, effective aggregation rules defeated the purpose of accurate regulation in one case where a nationwide approach *would* have been useful – the investigation and analysis of cross-jurisdictional aggregate data. The Commission declined to become involved and dropped the burden of investigation and analysis solely on local franchising authorities. The results illustrate both the inadequacy of the equipment aggregation rules and the urgent need for swift and effective enforcement tools to deal with cable operator intransigence.

B. Recommendations

One possible solution for the above problem would be for the Commission itself to review nationwide filings. To ensure that the accumulated expertise of prior rate review by local communities can be taken into account, however, such Commission review would need to incorporate cooperative features, such as mutual consultation with affected local communities or at the minimum a notice-and-comment process allowing input from franchising authorities and the public generally.

One approach that has not been tried in cable rate regulation is for the Commission to work together with local communities to unravel the intricacies of cable operator filings and arrive at a sound answer, rather than standing aloof from local attempts to apply the

[103] *Id.* at ¶ 5

Commission's rules and then judging the results in the manner of an appeals court Local communities seeking advice from the Commission on how to apply its rules, *prior* to issuing a rate order, have generally received little or no assistance or guidance. At times it appears the Commission regards local governments as coequal parties with the cable operators, to be treated as litigants, rather than as co-regulators seeking in good faith to apply the Commission's rules. A cooperative or partnership approach might be more helpful in arriving at accurate results.

It may be that the Commission would prefer not to get involved directly in the analysis of cable operator rate filings, even on a national basis. If so, a second alternative might be to require the cable operator who submits an aggregated filing to pay the cost of a third-party review of the filing and the supporting data by an independent accounting firm, selected and directed by the Commission, with input from local communities and the public as above. Presumably the cost savings an operator realizes through the aggregation of rate filings and consequent paperwork reduction would easily cover the cost of such a third-party review. The results could then be made available to all local franchising authorities that must rule on the individual filings.

In either case, it is important to reform the existing rules to prevent the sorts of abuses that have occurred to date. If the Commission intends to accept a sampling methodology, rather than an aggregation of ***all*** data in a category, it must specify the proper methodology for such sampling. It must require the operator to show that the methodology is revenue-neutral to the operator. More specifically, to the extent that the averaging involves a subsidy from some

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[104] *Id.*

communities to others, the operator should be required to show which communities realize the benefit of this subsidy and which are providing it -- so that there is some way to check on whether the averaging really is revenue-neutral.[105]

VI. THE COMMISSION'S APPROACH TO UNIFORM RATES RENDERS THE STATUTE POINTLESS AND ALLOWS ANTICOMPETITIVE PRACTICES.

A. Problem

The 1992 amendments to the Cable Act required an operator to have a uniform rate structure across the geographic area served by a cable system.[106] Initially, the Commission applied this requirement only where there was no effective competition.[107] Since the purpose of the uniformity requirement was to ensure that the benefits of any actual competition were applied throughout a cable system, that interpretation defeated the purpose of the statutory provision.[108] Thus, in early 1994 the Commission reconsidered and sought to apply the uniform rate provision in all franchise areas, irrespective of effective competition.[109] The D.C. Circuit, however, disagreed, and restricted the uniform rate provision to areas lacking effective competition.[110] That result was confirmed by the 1996 Act amendments, which added language

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[105] *See Richardson Reconsideration Order* at ¶ 18 (some subsidies necessarily result from the aggregation method).

[106] 47 U.S.C. § 543(d)

[107] *Rate Order* at ¶ 421

[108] ***See*** S. Rep. No. 102-92, at **76** (1991) ("Senate Report").

[109] *Third Reconsideration Order* at ¶ 24.

[110] *See Time Warner Entertainment.* 56 F.3d at 190-92

specifying that the provision did not apply "in any geographic area" where the operator is subject to effective competition.'"

The Commission generally appears to have read "geographic area" to mean "franchise area." As a result, entire franchise areas have been deregulated where only a portion is subject to effective competition. This has allowed cable operators to charge supracompetitive prices in other portions, as noted above.[112] However, nothing requires the Commission to assume that a "geographic area" must be a "franchise area."

B. Recommendations

As recommended above, the Commission can adopt a rule that allows actual ***competitive*** rates in nearby areas to be used to establish regulated rates in the non-competitive regions.[113] Such a rule would comply with the D.C. Circuit's decision and the 1996 amendments, because no regulated rate would be set in those geographic areas where actual competition exists. It would not be an implementation of the uniform rate provision, § 543(d), strictly speaking. It would regulate rates only in those areas where effective competition did not exist. But it would effect the intent of Congress by protecting subscribers in the non-competitive areas from supracompetitive rates.

In addition, the Commission needs to create effective rules to deal with predatory pricing and other anticompetitive practices. The Commission has already made some statements taking a stand against predatory pricing, primarily with respect to MDU bulk

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[111] 47 U.S.C. § 543(d)(1).

[112] ***See*** Section II.B.3 *supra*.

contracts."' But the examples mentioned above show that the present rules do not adequately prevent such practices.[115] Both for the sake of consumers, whom it must protect under the Cable Act, and for the sake of protecting competition itself from suppression through anticompetitive practices, the Commission needs to make explicit rules to prohibit practices by incumbents that stifle competition, covering single-family residential subscribers as well as MDUs. The Commission should also develop enforcement methods, in cooperation with local communities, that will afford prompt relief to those victimized by such practices.

VII. THE COMMISSION'S INACTION ON "COMMERCIAL" CABLE RATES HAS ALLOWED OPERATORS TO DISCRIMINATE AMONG SUBSCRIBERS.

A. Problem

The status of the "commercial rates" issue illustrates a key fact about rate regulation. The Commission's presentation of the issue in the *NPRM&O* treats the matter as "unresolved."[116] In fact, however, cable operators routinely charge subscribers they deem to be "commercial" at rate levels far in excess of the maximum permitted rates set under the Commission's rules. "Unresolved," to the industry, means that an operator can do as it chooses until the Commission specifically instructs it otherwise. Thus, when the Commission fails to resolve a problem, the result is not stasis; it is unrestrained abuse

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[113] ***Id***

[114] ***See, e.g.*, *Rate Order*** ¶ 424; ***Third Reconsideration Order*** at ¶¶ 18, 20; ***Effective Competition Order*** at ¶¶ 106-112.

[115] ***See*** n.40 ***supra.***

[116] *NPRM&O* at ¶ 30

The statute directs the Commission to protect "subscribers" from unreasonable rates, without distinguishing between residential and commercial subscribers Similarly, the Commission's actual present rules, as distinct from the questions raised by the Commission eight years ago, establish rules for subscriber rates without providing any exception for commercial subscribers. Local rate orders, too, generally do not provide commercial exceptions. And cable operators as a rule do not submit for rate review any separate "commercial" rates – only a single rate, presented as being calculated according to the Commission's regulations. It follows that, pending any Commission ruling to the contrary, cable operators must charge commercial subscribers the same regulated rates for basic service and equipment that they charge residential subscribers – *i.e.*, the one determined according to the FCC's rules to approximate the competitive rate.

Yet this is not the case. Subscribers alleged to be commercial are charged higher rates and may also be forced to accept other disadvantageous or anticompetitive terms to receive service. In the Portland, Oregon, metropolitan area, for example, commercial subscribers – both in multiple dwelling units (MDUs) and otherwise – are charged substantially higher rates than normal residential subscribers. These commercial subscribers are also required to sign multi-year contracts with the incumbent cable operator. The operators' exclusion of commercial rates from the process distorts the standard residential rate as well as allowing discrimination against so-called commercial subscribers, because neither the additional revenues operators extract from such subscribers, nor the real subscriber count, are properly incorporated in the rate calculations.

Various arguments may be made regarding commercial-residential discrimination. Some may suggest, for instance, that a sports bar can reasonably be charged higher rates than a home subscriber, on the grounds that the bar makes money because its customers can watch TV while imbibing or eating. The same may not be true, however, of a pediatrician's office that provides a television merely as an amenity in the waiting room. And the rationale appears to function quite differently in the case of, say, a trucking company that wishes to have the Weather Channel available for updates. It is clear that the vague term "commercial" may cover a multitude of possible uses of cable service by many types of cable subscribers.

In all these various cases, of course, the cable operator's basic tier costs are likely to be unchanged: the sports bar's hookup imposes no greater burden on an operator's cable system than the residential outlet.[117] So the industry's claim to charge higher rates to commercial subscribers does not appear to be based on costs.

There are more broadly disturbing aspects to the notion that a cable operator can discriminate among subscribers who receive the same service from the operator, based on the use they make of that service once received. To what extent are subscribers' First Amendment interests threatened by an assumption that a cable operator can monitor their activities and manipulate their pricing based on how they use the service'? Should the Commission allow cable operators to impose an essentially ungoverned "private regulation" scheme on their customers? It is already established that cable operators have an interest in controlling and

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[117] Indeed, when more people see the TV screen, this gives wider exposure to the cable operator's products - particularly if the operator's logo appears in ads or other announcements – and thus provides a sort of free advertising ("Say, I'd like to get this channel at home too . . .").

manipulating the way their subscribers are allowed to access information.[118] Allowing operators to make judgments about what subscribers are "commercial" and to charge them prices above the regulated (presumably competitive) rate approaches much closer to a federally-blessed private regulation regime than would be wise.

Yet, whether these arguments appear convincing or not, the fact is that operators are charging subscribers rates in excess of the maximum reasonable rates set according to Commission rules. And the Commission, having confused the issue by suggesting that it might someday adopt rules on separate commercial rates (a fact frequently restated, or overstated, by operators to local franchising authorities), has taken no steps to prevent this widespread, ten-year facial violation of the Commission's rules.

B. Recommendations

Unless and until the Commission adopts separate regulated rates for basic service and equipment for commercial subscribers, consistent with the congressional mandate of the statute, the Commission should clarify that operators must charge the same rates to commercial as to residential subscribers. If the Commission finds that there are cost differences in operators' provision of service to commercial and residential subscribers, then it may wish to

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[118] *See, e.g.*, Christopher Stern, *Comcast Halts Tracking of Its Subscribers; Privacy Activists Had Criticized Practice of Collecting Data on Visits to Web Sites*, Washington Post. Feb. 14, 2002, at E4; Brigitte Greenberg, *Privacy Complaints Prompt Change in Comcast Web Policy*, Communications Daily, Feb. 14, 2002.

allow for exceptions to this rule insofar as an operator can show the existence and amount of this cost."[119]

To allow enforcement of this rule, the Commission should permit any subscriber who has been discriminated against on "commercial rate" grounds to file a complaint directly with the Commission for relief, with a decision guaranteed within a short, specified time.[120] Alternatively, such a complaint could be filed with the local franchising authority, with the cable operator required (as noted above) to comply with a local rate order on the complaint unless and until the order was stayed or reversed by the Commission, and fines or forfeitures established for failure to do so.

VIII. CONCLUSION

As noted above, these Comments do not attempt to produce a complete catalogue of all the problems with, or potential improvements to, the rate regulation rules. It is to be hoped that the issues specifically discussed may serve as useful examples to assist the Commission in

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[119] If an operator alleges any difference in terms of programming costs, it should he required to show that this difference results from a legitimate arm's-length transaction with a programmer. Otherwise, the existing affiliations between programmers and cable operators could provide an easy avenue for collusive arrangements designed to enable operators to charge higher commercial rates. Operators should also be required to show that higher commercial revenues were not used either by the Commission, in its rules, or by the operator, in its Form 393 and 1200 filings, to establish the initial regulated rates.

[120] To date, Commission rulings on rate appeals have provided an outstanding example of the maxim that "justice delayed is justice denied." For example, the Commission's appeal decision regarding the Fairfield Ohio system represented a three-year delay. *In re TCI Cablevision of Ohio, Inc., Appeal of Local Rate Order of the City of Fairfield, Ohio*, Memorandum Opinion and Order, 13 FCC Rcd. 17,303, ¶ 1 (1998) (rate order adopted June 12, 1995. appeal filed July 12, 1995, appeal decision issued July 1, 1998).

identifying and correcting other problems, and in evaluating the suggestions that will be made by the cable industry to minimize the effectiveness of the Commission's rules.

One fact that becomes evident from the above discussion must be reemphasized. The Commission *cannot* rely on the industry to police itself, to voluntarily accept reasonable rates, or to comply with the "spirit" of the Commission's rules in good faith. History shows otherwise. In other words, if the Commission does not enforce sound rate rules, rates *will* he unreasonable. It follows that, unwelcome as the task of dealing with rate rules may be, the statutory mandate means that the Commission must take affirmative steps to stop evasions and to make sure its rules work as they should.

Similarly, it is essential for the Commission to realize that enforcing reasonable rates is not a punishment. Being forced to charge a reasonable rate is not a burden on a cable operator. Rather, rate rules are merely intended to reproduce an approximation of what the cable operator *would* have to do in any case if there were real, working competition. Thus, it would be inappropriate to justify allowing any unreasonable rates on the grounds that the cable operator should not be "punished" for "honest mistakes." (If the Internal Revenue Service took that approach, few taxpayers would ever pay interest or penalties for errors on tax returns.) Even if mistakes are honest, they are *mistakes;* and legitimizing them automatically means allowing unreasonable, supracompetitive rates for subscribers.

The Commission may not, consistent with its legal obligations, permit its rules to be misused or abused. It may correct such misuses kindly, if it believes an honest mistake has been made in a particular individual case because a rule was truly confusing and Commission guidance was not forthcoming; but it must correct them.

For the reasons indicated above, the Bureau should revise and enforce its rate rules as recommended herein.

Respectfully submitted,

Frederick E. Ellrod III

Nicholas P. Miller
Frederick E. Ellrod III
Mitsuko R. Herrera
Miller & Van Eaton, P.L.L.C.
1155 Connecticut Avenue, N.W. #1000
Washington, D.C. 20036-4306
202-785-0600

Counsel for the National Association of Telecommunications Officers and Advisors, the National League Of Cities, and the Miami Valley Cable Council

November 4, 2002

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EXHIBIT 1

DECLARATION OF GARTH ASHPAUGH, CPA

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
Revisions to Cable Television Rate Regulations	)	MB Docket No. 02-144
Implementation of Sections of The Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation	)	MM Docket No. 92-266
Implementation of Sections of The Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation	)	MM Docket No. 93-215
Adoption of a Uniform Accounting System for the Provision of Regulated Cable Service	)	CS Docket No. 94-28
Cable Pricing Flexibility	)	CS Docket No. 96-157

DECLARATION OF GARTH ASHPAUGH IN SUPPORT OF THE COMMENTS OF THE NATIONAL ASSOCIATION OF TELECOMMUNICATIONS OFFICERS AND ADVISORS, THE MIAMI VALLEY CABLE COUNCIL

I, Garth T. Ashpaugh, declare as follows:

1. I submit this declaration in support of the comments submitted by the National Association of Telecommunications Officers and Advisors, ***et.*** *al,* in the above-captioned matter. I am fully competent to testify to the facts set forth herein, and if called as a witness, I would testify to them.

2. I have served as President and Member of Ashpaugh & Sculco, CPAs, PLC, since December 1999. I am licensed as a Certified Public Accountant in the states of Florida and Missouri. I previously served as an Audit Supervisor for the Missouri Public

Service Commission. I earned my Bachelor's of Science in Business Administration from the University of Missouri in 1977.

3. I have over twenty years of experience in cable and utility rate regulation matters. Since 1992, I have worked with over 200 cities and counties in cable-related matters. I have performed financial analyses and audits of cable operator rate and equipment filings, renewal proposals, and transfer applications in Arizona, California, Florida, Kentucky, Maryland, Michigan, Minnesota, New Mexico, New York, Ohio, Pennsylvania, Tennessee, Texas, Virginia, Wisconsin and Wyoming. I have also assisted clients in evaluating mergers and purchases including Kansas City Power and Light and UtiliCorp, Baltimore Gas and Electric Company and Potomac Electric Power Company, SBC Media and Prime Communications, Prime Communications and Comcast, AT&T Communications and Tele-Communications Inc., and AT&T Broadband and Comcast Communications.

4. I have reviewed national equipment rate filings submitted by AT&T and Time Warner. In both situations, the operators were reluctant to work with the local communities to resolve rate regulation issues. For example, all of the AT&T equipment rate information was calculated by the AT&T Denver office. In response to specific questions that I submitted on behalf of a single community, AT&T sent thousands of documents which then had to be reviewed by the community at substantial expense. In addition, like many operators, AT&T required the community to keep the reviewed information confidential. When AT&T was notified of certain errors or corrections, AT&T did not correct similar filings that it had submitted to other communities. Because of the confidentiality agreement, the reviewing community could not share information

with other communities. Thus, every AT&T-served community with rate regulation authority was in effect required to perform separate, expensive reviews of substantially similar documents to ascertain information that AT&T should have provided initially.

5. Time Warner's 2001 FCC Form 1205 equipment filings provide another example of an operator's attempt to prevent a community from reviewing aggregate equipment rate calculations. Time Warner has each of its fifty participating systems compile data specific to each area and send the information to Time Warner's Connecticut office. There it is "consolidated" with minor changes to reflect efforts at consistency. However, my review revealed that there is very little consistency in the methodologies of the 50 systems. Some systems properly allocated costs to the FCC Form 1205, *e.g.*,, the portion of installation costs properly allocable to subscribers, and then allocated costs from FCC Form 1205 to the equipment basket. Other systems did not calculate what portion of costs were not properly allocable to FCC Form 1205, *e.g.*, the cost of installation wiring on the cable operator side of the cable wiring demarcation point, and instead improperly allocated 100% of costs to the equipment basket. Some systems included capitalized installations in the equipment basket, while others did not. Given the **lack** of uniform methodology, Time Warner's consolidated aggregate equipment rate calculations are unreliable at best.

6. After seven months of asking for Time Warner for detailed support and not receiving any responses to any of the community's questions (other than a box of work papers with no cover letter and no explanations), Time Warner delivered to my office, without any further notice, the original documents received by the Connecticut office concerning the 2001 consolidated FCC Form 1205 filing. The cover letter stated if I had

any further questions I should contact each of the fifty systems individually. I was not provided any contact information for the fifty systems – no names, phone numbers or e-mail addresses. As there were at the time only six weeks left within the community's twelve-month review period, Time Warner had effectively run out the clock on the community's ability to challenge Time Warner's questionable national equipment rate averaging practices.

7. In addition, in Time Warner's 2002 FCC Form 1205 filing for the Miami Valley [Ohio] Cable Council, Time Warner filed a regional equipment rate filing with substantially higher equipment rates as compared to Time Warner's 2002 national FCC Form 1205 filing. There is no evidence that Time Warner excluded the higher Miami Valley regional equipment rates in preparing its national average equipment rates. Thus, when the national equipment rate filing is provided to other communities, those communities must pay higher rates because of the inclusion of certain higher regional rates, yet subscribers living in communities in regions with higher regional rates are not receiving the benefit of lower, nationally averaged rates.

I declare under penalty of perjury that the foregoing **is** true and correct to the best of my knowledge and belief, and that this declaration **was** executed on November **3,** 2002, at Winter **Park,** Florida.

Garth T. Ashpaugh

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